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Nos. 80-1684, 80-1691, and 80-1802

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & CO., *et al.*, *Petitioners*,

v.

WACHOVIA BANK & TRUST CO., N. A., *et al.*, *Respondents*.

BRIEF FOR THE RESPONDENTS IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether a private action for fraud under Section 10(b) of the Securities Exchange Act of 1934 must be brought within the statutorily prescribed time for a private action for negligence under Section 12(2) of the Securities Act of 1933.

2. Whether fraud remedies under Section 10(b) are available only to sellers of securities and do not extend to defrauded purchasers.

3. Whether accountants and attorneys who actively participate in a fraud are excluded from the definition of "any person" in Section 10(b).

4. Whether fraudulent conduct not covered by express liability provisions of the federal securities laws is nevertheless also excluded from the coverage of the "catch-all" fraud provisions of Section 10(b).

5. Whether investors who participate in the securities markets through institutional fiduciaries are entitled to less protection under Section 10(b) than other investors.

6. Whether a decision overruling clear and previously controlling precedent by shortening the statute of limitations for bringing an action under Section 10(b) must be applied retroactively even when such application would be substantially inequitable.

TABLE OF CONTENTS

	PAGE:
OPINIONS BELOW	1
JURISDICTION	2
STATEMENT	2
ARGUMENT	9
CONCLUSION	24

TABLE OF AUTHORITIES

CASES:	PAGE
Aaron v. *SEC*, 446 U.S. 680 (1980)	9
Aboussie v. *Aboussie*, 441 F.2d 150 (5th Cir. 1971)	20
Adickes v. *S. H. Kress & Co.*, 398 U.S. 144 (1970)	10
Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972)	9, 17
Andrus v. *Allard*, 444 U.S. 51 (1979)	14
Azalea Meats, Inc. v. *Muscat*, 246 F. Supp. 780 (S.D. Fla. 1965), rev'd on other grounds, 386 F.2d 5 (5th Cir. 1967)	20
Bailes v. *Colonial Press, Inc.*, 444 F.2d 1241 (5th Cir. 1971)	20
Baumel v. *Rosen*, 283 F.Supp. 128 (D. Md. 1968)	19
Berry Petroleum Co. v. *Adams & Peck*, 518 F.2d 402 (2d Cir. 1975)	21
Blau v. *Lehman*, 368 U.S. 403 (1962)	14
Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975)	9, 12, 14
Butterman v. *Steiner*, 343 F.2d 519 (7th Cir. 1965)	20
Cahill v. *Ernst & Ernst*, 625 F.2d 151 (7th Cir. 1980)	11
Campbell v. *Haverhill*, 155 U.S. 610 (1895)	11

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Table of Authorities Continued

CASES: PAGE

Cannon v. *University of Chicago,* 441 U.S. 677 (1979) 9, 13

Carothers v. *Rice,* 633 F.2d 7 (6th Cir. 1980), cert. denied, 49 U.S.L.W. 3710 (Mar. 23, 1981) 11

Carpenter v. *Hall,* 311 F. Supp. 1099 (S.D. Tex. 1970) .. 20

Charney v. *Thomas,* 372 F.2d 97 (6th Cir. 1967) 20

Chevron Oil Co. v. *Huson,* 404 U.S. 97 (1971) 8, 21, 22

Chiodo v. *General Waterworks Corp.,* 380 F.2d 860 (10th Cir.), cert. denied, 389 U.S. 1004 (1967) 20

Conlow v. *University Computing Co.,* [1972-1973] Fed. Sec. L. Rep. (CCH) ¶ 93,796 (D.D.C. 1973) 21

Connelly v. *Balkwill,* 174 F. Supp. 49 (N.D. Ohio 1959), aff'd per curiam, 279 F.2d 685 (6th Cir. 1960) 20

Cook v. *Avien, Inc.,* 573 F.2d 685 (1st Cir. 1978) 11, 21

Cort v. *Ash,* 422 U.S. 66 (1975) 8

Dack v. *Shanman,* 227 F. Supp. 26 (S.D.N.Y. 1964) 19

deHaas v. *Empire Petroleum Co.,* 435 F.2d 1223 (10th Cir. 1970) 20

Denny v. *Performance Systems, Inc.,* [1971-1972] Fed. Sec. L. Rep. (CCH) ¶ 93,387 (M.D. Tenn. 1971) ... 20

Douglas v. *Glenn E. Hinton Investments, Inc.,* 440 F.2d 912 (9th Cir. 1971) 20

Dudley v. *Allen,* [1971-1972] Fed. Sec. L. Rep. (CCH) ¶ 93,273 (W.D. Ky. 1971) 20

Ernst & Ernst v. *Hochfelder,* 425 U.S. 185 (1976) 9, 10, 11

Errion v. *Connell,* 236 F.2d 35 (9th Cir. 1971) 20

Firestone Tire & Rubber Co. v. *Risjord,* 49 U.S.L.W. 4089 (Jan. 13, 1981) 23

Table of Authorities Continued

CASES:	PAGE
Fischman v. *Raytheon Manufacturing Co.*, 188 F.2d 783 (2d Cir. 1951)	19
Forrestal Village, Inc. v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977)	8, *passim*
Fratt v. *Robinson*, 203 F.2d 627 (9th Cir. 1953)	20
Geo. H. McFadden & Brothers v. *Home-Stake Production Co.*, 295 F. Supp. 587 (N.D. Okla. 1968)	20
Glickman v. *Schweickart & Co.*, 242 F. Supp. 670 (S.D.N.Y. 1965)	19
Hecht v. *Harris, Upham & Co.*, 283 F. Supp. 417 (N.D. Cal. 1968), modified on other grounds, 430 F.2d 1202 (9th Cir. 1970)	20
Heit v. *Weitzen*, 402 F.2d 909 (2d Cir. 1968), cert. denied, 395 U.S. 903 (1969)	17
Hendricks v. *Flato Realty Investments*, [1967-1969] Fed. Sec. L. Rep. (CCH) ¶ 92,290 (S.D. Tex. 1968)	20
Hooper v. *Mountain States Securities Corp.*, 282 F.2d 195 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961)	20
Holzsager v. *The Valley Hospital*, No. 80-7839 (2d Cir. Apr. 10, 1981)	23
Hudak v. *Economic Research Analysts Inc.*, 499 F.2d 996 (5th Cir.), cert. denied, 419 U.S. 1122 (1974)	11
Huddleston v. *Herman & MacLean*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 97,919 (5th Cir. 1981)	13
IIT v. *Cornfeld*, 619 F.2d 909 (2d Cir. 1980)	11
Janigan v. *Taylor*, 344 F.2d 781 (1st Cir.), cert. denied, 382 U.S. 879 (1965)	19
Johnson v. *Railway Express Agency, Inc.*, 421 U.S. 454 (1975)	11
Klein v. *Auchincloss, Parker & Redpath*, 436 F.2d 339 (2d Cir. 1971)	19

Table of Authorities Continued

CASES:	PAGE
Klein v. *Bower*, 421 F.2d 338 (2d Cir. 1970)	19
Klein v. *Spear, Leeds & Kellogg*, 306 F. Supp. 743 (S.D.N.Y. 1969)	19
Lehigh Valley Trust Co. v. *Central National Bank of Jacksonville*, 409 F.2d 989 (5th Cir. 1969)	18
Lorillard v. *Pons*, 434 U.S. 575 (1978)	14
Maher v. *J.R. Williston & Beane, Inc.*, 280 F. Supp. 133 (S.D.N.Y. 1967)	19
Marth v. *Industrial Incomes Incorporated of North America*, 290 F. Supp. 755 (S.D.N.Y. 1968)	19
McCluny v. *Silliman*, 28 U.S. (3 Pet.) 270 (1830)	11
Mills v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970)	18
Mitchell v. *Texas Gulf Sulphur Co.*, 446 F.2d 90 (10th Cir.), cert. denied, 404 U.S. 1004 (1971)	12, 20
Moerman v. *Zipco, Inc.*, 302 F. Supp. 439 (E.D.N.Y.), aff'd per curiam, 422 F.2d 871 (2d Cir. 1970)	19
Morgan v. *Koch*, 419 F.2d 993 (7th Cir. 1969)	20
National Realty Trust v. *Neelon Management Co.*, [1973] Fed. Sec. L. Rep. (CCH) ¶ 94,049 (D.D.C. 1973)	20-21
NLRB v. *Sears, Roebuck & Co.*, 421 U.S. 132 (1975)	18
Northern Trust Co. v. *Essaness Theatres Corp.*, 103 F. Supp. 954 (N.D. Ill. 1952)	20
Occidental Life Ins. Co. of California v. *EEOC*, 432 U.S. 355 (1977)	12
O'Hara v. *Kovens*, 625 F.2d 15 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981)	21
Osborne v. *Mallory*, 86 F. Supp. 869 (S.D.N.Y. 1949)	19
Parrent v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972)	21

Table of Authorities Continued

CASES:	PAGE
Piper v. *Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977)	9
Ramsey v. *United Mine Workers*, 401 U.S. 302 (1971)	18
Richardson v. *MacArthur*, 451 F.2d 35 (10th Cir. 1971)	20
Roberts v. *Magnetic Metals Co.*, 611 F.2d 450 (3rd Cir. 1979)	11
Ross v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980)	13, 16, 17
Royal Air Properties, Inc. v. *Smith*, 312 F.2d 210 (9th Cir. 1962)	20
Rubin v. *United States*, 101 S.Ct. 698 (1981)	18
Sackett v. *Beaman*, 399 F.2d 884 (9th Cir. 1968)	20
Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977)	9
Saylor v. *Lindsley*, 302 F. Supp. 1174 (S.D.N.Y. 1969)	19
Schaefer v. *First National Bank of Lincolnwood*, 326 F. Supp. 1186 (N.D. Ill. 1971)	20
Schaefer v. *First National Bank of Lincolnwood*, 509 F.2d 1287 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976)	22
SEC v. *National Securities Co.*, 393 U.S. 453 (1969)	18
SEC v. *National Student Marketing Corp.*, 457 F. Supp. 682 (D.D.C. 1978)	2, 6
Shapiro v. *Schwamm*, 279 F. Supp. 798 (S.D.N.Y. 1968)	19
Smith v. *Guaranty Service Corp.*, 51 F.R.D. 289 (N.D. Cal. 1970)	20
Stevens v. *Abbott, Proctor & Paine*, 288 F. Supp. 836 (E.D. Va. 1968)	20
Superintendent of Insurance v. *Bankers Life & Casualty Co.*, 404 U.S. 6 (1971)	9, 17
Tobacco & Allied Stocks, Inc. v. *Transamerica Corp.*, 143 F. Supp. 323 (D. Del. 1956), aff'd without consideration of the point, 244 F.2d 902 (3rd Cir. 1957)	19

Table of Authorities Continued

CASES: PAGE

Touche Ross & Co. v. *Redington,* 442 U.S. 560 (1979) 8, 9, 14

Transamerica Mortgage Advisors, Inc. v. *Lewis,* 444 U.S. 11 (1979) 8, 14

Trussell v. *United Underwriters, Ltd.,* 228 F. Supp. 757 (D. Colo. 1964) 20

Turner v. *Lundquist,* 377 F.2d 44 (9th Cir. 1967) 20

UAW v. *Hoosier Cardinal Corp.,* 383 U.S. 696 (1966) .. 11

United California Bank v. *Salik,* 481 F.2d 1012 (9th Cir.), cert. denied, 414 U.S. 1004 (1973) 11

United States v. *Naftalin,* 441 U.S. 768 (1979) 17, 18

United States v. *Natelli,* 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976) 2, 4

Valencia v. *Anderson Brothers Ford,* 617 F.2d 1278 (7th Cir.), cert. granted, 101 S.Ct. 395 (1980) 23

Vance v. *National Realty Trust,* [1974-1975] Fed. Sec. L. Rep. (CCH) ¶ 95,004 (D.C. Cir. 1975) 20

Vanderboom v. *Sexton,* 422 F.2d 1233 (8th Cir.), cert. denied, 400 U.S. 852 (1970) 11

Weinberger v. *New York Stock Exchange,* 335 F. Supp. 139 (S.D.N.Y. 1971) 19

Weiser v. *Shwartz,* 286 F.Supp. 389 (E.D. La. 1968) 20

STATUTES:

Investment Advisers Act of 1940 §206, 15 U.S.C. 80b-6 14

Securities Act of 1933

§11, 15 U.S.C. 77k 11

§12, 15 U.S.C. 77l ..... 7, *passim*

§17, 15 U.S.C. 77q 18

Table of Authorities Continued

STATUTES: PAGE

Securities Exchange Act of 1934

§3(a)(9), 15 U.S.C. 78c(a)(9) 15

§10(b), 15 U.S.C. 78j(b) ..... 3, *passim*

§17, 15 U.S.C. 78q 14

§18, 15 U.S.C. 78r ..... 7, *passim*

MISCELLANEOUS:

H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. (1934).. 15

R. Stern & E. Gressman, Supreme Court Practice (5th ed. 1978) 23

IN THE

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PEAT, MARWICK, MITCHELL & CO., *et al., Petitioners,*

v.

WACHOVIA BANK & TRUST CO., N. A., *et al., Respondents.*

BRIEF FOR THE RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A)[1] is not yet officially reported. The opinion of the district court in Nos. 80-1684 and 80-1691 (Pet. App. B) is reported at 461 F.

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[1] Unless otherwise indicated, the designation "Pet." refers to the petition for a writ of certiorari in No. 80-1691. The designation "Pet. App." refers to the appendix in that petition.

Supp. 999. The opinion of the district court in No. 80-1802 (No. 80-1802, Pet. App. A) is not officially reported.

JURISDICTION

The judgment of the court of appeals was entered on December 5, 1980. Petitions for rehearing and suggestions for rehearing *en banc* were denied on March 4, 1981. (Pet. App. C). Petitions for a writ of certiorari were filed on April 7, 1981, April 8, 1981, and April 29, 1981. The jurisdiction of this court is invoked under 28 U.S.C. §1254(1).

STATEMENT

This case arises from the financial debacle of the National Student Marketing Corporation ("NSMC") in the late 1960's. Following that debacle, successful criminal actions were brought against certain officers of NSMC and a partner of the accounting firm in this action (Petitioner Natelli).[2] In addition, an SEC injunctive action resulted in consent judgments against the Petitioners now before this Court.[3] Nevertheless, for nearly a decade the victims of the fraud have been deprived of their day in court. Petitioners now attempt to make that deprivation permanent by seeking certiorari from the refusal of the court of appeals to uphold dismissal of the complaint in this action.

Respondents, plaintiffs below, are Wachovia Bank and Trust Co., N. A., Mellon Bank, N. A., First Wisconsin Trust

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[2] *See United States* v. *Natelli*, 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976). Petitioner Scansaroli, the other individual accountant in this action, also was indicted and was convicted of violations of the federal securities laws in this matter. However, his conviction was overturned on appeal. The court of appeals found that there was sufficient evidence to convict Scansaroli of criminal law violations, but that it could not be determined if the jury had in fact convicted him of a violation for which there was insufficient evidence. Mr. Scansaroli was never re-tried after remand.

[3] *See SEC* v. *National Student Marketing Corp.*, 457 F. Supp. 682, 687 n.2 (D.D.C. 1978).

Co., the Dreyfus Offshore Trust, N. V. and National Fire Insurance Co. of Hartford. On December 17, 1969, they purchased more than $5 million of NSMC stock from NSMC and two of its directors in a private placement. Three of the five Respondents purchased their NSMC shares as fiduciaries for employee retirement plans and other trust accounts. The price was negotiated from the prevailing market to reflect long term restrictions against resale. The stock turned out to be virtually worthless.

Petitioners, defendants below, are Peat, Marwick, Mitchell & Co. ("PMM"), a national accounting firm that regularly acted as NSMC's independent auditors; Anthony M. Natelli, the PMM partner in charge of the NSMC account; Joseph Scansaroli, PMM's audit supervisor of the NSMC account; White & Case, a New York law firm that regularly represented NSMC as outside counsel and served as such in connection with the private placement involving the Respondents; Marion Jay Epley, III, the White & Case partner principally responsible for the NSMC account; and certain former NSMC officers and directors. NSMC was also named as a defendant in the original complaint; however, it subsequently settled with the plaintiffs.

Respondents' complaint, as amended, alleges that the Petitioners violated and aided and abetted violations of Section 10(b) in connection with NSMC's dissemination of false and misleading statements in the marketplace. These false statements, going to the very heart of NSMC's financial condition, were disseminated to investors orally, in press releases, and in numerous public announcements and reports. The great majority were made orally and in documents that were not filed with the SEC (Complaint, Paras. 22, 24, 25, 26, 30, 31, 53, 55, 57, 59, 63, 66, 69). Their effect was to inflate artificially the price of NSMC stock, which was then used fraudulently to acquire numerous profitable corporations. The earnings of these corporations were then pooled with NSMC's to mask the fact that NSMC itself was losing money at a staggering rate.

The accounting Petitioners and the attorney Petitioners were not mere peripheral defendants caught up in a fraudulent scheme of which they had no knowledge. Rather, they were critical participants in that scheme who knew what was transpiring and deliberately chose to further the deception of their client.

Through late 1968, NSMC's scheme to defraud was accomplished principally through the booking of revenues from so called "commitments" to purchase NSMC services ("unbilled sales"). These commitments were first booked in connection with NSMC's 1968 year end audit when PMM learned that a trial balance showed more than a $200,000 loss for the year. PMM then allowed NSMC retroactively to book $1.7 million of revenues from "commitments" even though (1) not a single dollar from these commitments was received prior to year end; (2) PMM did not confirm the existence of the commitments with NSMC's customers; and (3) PMM knew that there were no written contracts for virtually all of the commitments. When in 1969 the great majority of the commitments had failed to materialize and had to be written off, PMM concealed the effect of these write-offs by permitting NSMC to substitute a series of new non-existent commitments. As the Second Circuit found in *United States* v. *Natelli*, 527 F.2d 311, 319 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976):

> "The original action of Natelli in permitting the booking of unbilled sales after the close of the fiscal period in an amount sufficient to convert a loss into a profit was contrary to sound accounting practice. . . . When the uncollectibility, and indeed, the non-existence of these large receivables was established in 1969, the revelation stood to cause Natelli severe criticism and possible liability. He had a motive, therefore, intentionally to conceal the write-offs that had to be made."

PMM, notwithstanding its knowledge of the fraud, rendered unqualified opinions upon NSMC's financial statements and assisted in the preparation of NSMC's interim financial

statements which it knew were false. For that reason, NSMC was able to report dramatic increases in sales and earnings from one accounting period to the next even though such sales and earnings increases were wholly chimerical.

The widespread dissemination of false reports of increasing sales and earnings served to excite the market and artificially inflate the price of NSMC stock. In less than two years NSMC stock climbed from $6 a share to $144 a share even though the company was in fact losing money during this entire period.[4] By early 1969, however, NSMC was unable to generate enough fraudulent "commitments" to maintain its reports of spectacular growth. Accordingly, it embarked on a series of fraudulent corporate acquisitions in which it used its inflated stock and false financial statements to purchase profitable companies. NSMC then pooled the earnings of the profitable companies with its own and thereby concealed the write-offs of commitments that had failed to materialize.

During NSMC's corporate acqusition program, Respondents purchased for cash more than $5 million of NSMC stock. The purchases were effected through Common Stock Purchase Agreements. Under the agreements, Respondents' obligation to purchase NSMC shares was conditioned on receipt from White & Case of a legal opinion to the effect that, among other things, consummation of the transaction would not result in a violation of any statute, rule or regulation. White & Case and Epley rendered such legal opinions to each of the Respondents without any qualification.

In fact, as Epley well knew, the sales to Respondents resulted in numerous violations of the securities laws because they were based on false representations. Epley knew of the fraud because he had been a central participant in the fraudulent transactions which gave rise to the false representations.

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[4] The $144 figure takes into account a two-for-one stock split.

For example, Epley had served as NSMC's counsel in the October 1969 merger of Interstate National Corporation into NSMC — the principal subject of the SEC's enforcement action in *SEC* v. *National Student Marketing Corp.*, 457 F. Supp. 682 (D.D.C. 1978). There, prior to the closing, the head of PMM's SEC Review Committee called Epley to advise him that NSMC's most recent nine-month financials must be corrected to show a $180,000 loss instead of the $700,000 profit shown in the financial statements used to obtain shareholder approval of the merger. Epley declined to inform Interstate of this development, but falsely represented to PMM that he had discussed the matter with Interstate and Interstate still wanted to go forward. The merger was closed only on Epley's fraudulent representation to Interstate that an unsigned, incomplete draft comfort letter from PMM regarding the most recent nine-month financials was in fact final and complete, and that a signed copy would be forthcoming from PMM. The final comfort letter, which Epley never disclosed to Interstate, not only contained the qualification that NSMC had lost $180,000, but also stated that Interstate should consider a resolicitation of shareholders with corrected financials prior to closing.

The following month Epley and White & Case represented NSMC in three more fraudulent acquisitions. In each instance, White & Case prepared representations that the nine-month financials — which Epley knew from the Interstate transaction were false — were "true and correct" and "prepared in accordance with generally accepted accounting principles." At no time did Epley disclose the infirmities with the Interstate acquisition to the companies that were later being acquired on the basis of Interstate earnings. As a result, NSMC was able to use its false financial statements and inflated stock to perpetuate its fraud by acquiring new companies with profits that could be used to conceal NSMC's losses in NSMC's consolidated financial statements. Of course, the paper empire that NSMC had built with the assistance of its professional advisers was largely dismantled

through a series of rescission actions instituted after the fraud was discovered.

In the courts below the defendants urged that no private right of action exists under Section 10(b) of the Securities Exchange Act for the fraud charged. They argued that recognition of a claim under Section 10(b) would "nullify the express provisions of the 1933 Act" (PMM Court of Appeals Brief, p. 67), and that "an Implied Right of Action Does Not Lie Since the Conduct in Issue Is Subject to §18 [of the Securities Exchange Act]" (id at 68). Defendants also moved to dismiss the action as time-barred under the District of Columbia's two-year blue-sky statute of limitations. Defendants' motion to dismiss was made more than four years after the filing of plaintiffs' complaint, by which time no fewer than 166 witnesses had been deposed and plaintiffs had been compelled to produce, copy and analyze literally hundreds of thousands of documents.

The district court rejected defendants' contention that no claim for relief was stated under Section 10(b). It found that plaintiffs were alleging a cause of action far different from that addressed by Section 12(2) of the Securities Act or Section 18(a) of the Securities Exchange Act — the two express provisions defendants relied upon to argue there was no claim under Section 10(b). With respect to Section 18(a), the court noted that "plaintiffs have alleged materially false statements which were never contained in a document filed with the SEC and thus are clearly exempt from §18(a) liability" (Pet. App. B-8). Further, "[w]ith limited exceptions, plaintiffs do not allege reliance upon documents filed with the SEC and, contrary to the position of defendants, such reliance is essential to recovery under §18(a)" (ibid). With respect to Section 12(2), the court stated that victims of intentional fraud are not limited to the Section 12(2) negligence remedy, and further that "there is some question whether [Section 12(2)] applies to the present defendants since they were not 'sellers' of the securities in question" (id at B-8).

The district court, however, dismissed the complaint as time-barred under the District of Columbia's two-year blue sky statute of limitations. The court relied on the 1977 decision of the District of Columbia Circuit in *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (1977), which broke with past precedent and applied the two-year blue-sky limitation period instead of the three-year general fraud limitation period. At the time plaintiffs had filed their complaint in January 1973, the three year general fraud statute applied to Section 10(b) actions brought in the District of Columbia.

The court of appeals reversed the dismissal. With respect to the existence of a private right of action under Section 10(b), the court noted that in the last decade this Court has acknowledged that a private right of action exists under Section 10(b) in no less than six cases (Pet. App. A-18 and n. 21). It found that such recognition was consistent with the four-part test in *Cort* v. *Ash*, 422 U.S. 66, 78 (1975), and that neither *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979) nor *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 (1979) compelled a different result. It rejected what it characterized as defendants' "Catch 22" argument based on express remedies, noting that although defendants urged that the existence of express remedies precluded a remedy under Section 10(b), "in each instant [defendants] are at the ready to show that the express remedies are not really available to Wachovia" (Pet. App. A-26). It further pointed out that these express remedies "are totally different from the remedy implied under Section 10(b), and . . . are meant to treat different problems and to be applied in different situations" (Pet. App. A-27).

On the question of prospective application of the statute of limitations decision, the court followed this Court's decision in *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971). It found that its *Forrestal Village* decision overruled the law in the District of Columbia Circuit at the time plaintiffs filed the complaint, that the three-year general fraud statute applied to Section 10(b) actions. It noted that as of the time the lower

court found the blue sky limitation period had expired, forty-six of forty-eight federal court decisions had applied the forum state's general fraud statute of limitations to Section 10(b) actions, and that as late as 1975 — two years after the complaint was filed — D. C. decisions were still applying the three year general fraud statute to Section 10(b) actions. It found that to hold that Respondents slept on their rights would produce "substantial inequitable results," since they could not have known that the statute of limitations in effect at the time they filed their complaint would be shortened in a decision still years down the road.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this court or any other court of appeals. Further review is therefore unwarranted.

1. The court of appeals created no new remedy. Rather it reconfirmed the well-established private claim for relief under Section 10(b). That claim has been recognized in countless federal court decisions over the last thirty-five years, and has been confirmed by this Court in numerous recent decisions.[5] Further, the court of appeals did not extend Section 10(b) to a new class of plaintiffs, to a new type of fraud, or to a new category of defendants. It held only that purchasers of securities who are victims of a massive but essentially garden-variety fraud have a remedy under Section 10(b) against persons who, acting with *scienter*, make materially false and

[5] *See Aaron* v. *SEC*, 446 U.S. 680, 689 (1980); *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 569, 577 n.19 (1979); *Cannon* v. *University of Chicago*, 441 U.S. 677, 692 n.13, 706 n.40 (1979); *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977); *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 25 (1977); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 196 (1976); *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 730 (1975); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 144-154 (1972); *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 13 n.9 (1971).

misleading representations in connection with the sale of securities.

Petitioners attack the lower court's recognition of a Section 10(b) remedy on several grounds. None reflects a conflict in the circuits or a conflict with any decision of this Court.

2. The attorney Petitioners principally argue that purchasers should not to able to bring a fraud action under Section 10(b) once the time has expired for bringing a negligence action under Section 12(2) of the Securities Act, a section which does not even apply to them. (Pet. i, 11-16). This novel argument was not addressed by the lower courts because Petitioners did not there advance it. In the lower courts, Petitioners argued that the D.C. blue-sky limitation period governs, not the statute of limitations that governs Section 12(2). Ordinarily, a litigant will not be heard to assert in this Court contentions which it did not raise below. See, e.g., *Adickes* v. *S.H. Kress & Co.*, 398 U.S. 144, 147 n.2 (1970).

Further, Petitioners' argument in this Court is simplistic. They contend that the Section 10(b) remedy nullifies the procedural constraints in Section 12(2) because a longer statute of limitation could be applied to Section 10(b). Petitioners ignore, however, that Section 10(b) and Section 12(2) treat different problems and apply in different situations; hence, reliance on the former does not in any way nullify or undermine the latter. This is particularly true where, as here, the Petitioners are not even sellers and thus cannot be reached by a Section 12(2) action.

Section 10(b) is directed to fraud, and a plaintiff who elects to proceed under Section 10(b) undertakes the burden of proving *scienter*. *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976). Section 12(2) is simply a misrepresentation statute. *Scienter* is irrelevant, and indeed a plaintiff can establish a prima facie case by simply showing a misrepresentation and forcing the defendants to prove an affirmative defense of non-negligence.

Given the burden on a plaintiff in a Section 10(b) action to prove *scienter*, it can hardly be argued that recognition of an action under Section 10(b) would nullify Section 12(2). Indeed, in *Ernst & Ernst* v. *Hochfelder, supra*, 425 U.S. at 210, this Court recognized that imposition of a *scienter* requirement under section 10(b) was necessary to avoid nullification of the procedural restrictions in Section 12(2), as well as in the other express remedies of the securities laws.[6]

Further, Petitioners ignore the fact that for more than a century this Court has instructed lower courts that where no federal statute of limitations is provided for a particular cause of action, the federal courts are not to borrow other federal limitation periods but are to utilize the appropriate limitation period of the forum state.[7] In *Hochfelder*, this Court noted that such use of state statutes of limitations is the practice in Section 10(b) cases. 425 U.S. at 210 n. 29. Every single court of appeals in the federal system applies state limitation periods to Section 10(b) actions.[8]

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[6] The express remedies of the securities laws generally place the burden on the defendant to prove absence of culpability. See, e.g., Sections 11(b) and 12(2) of the Securities Act and Section 18(a) of the Securities Exchange Act.

[7] *See, e.g., Johnson* v. *Railway Express Agency, Inc.*, 421 U.S. 454, 462 (1975); *UAW* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 701-704 (1966); *Campbell* v. *Haverhill*, 155 U.S. 610, 621 (1895); *McCluny* v. *Silliman*, 28 U.S. (3 Pet.) 270, 277 (1830).

[8] *Cook* v. *Avien, Inc.*, 573 F.2d 685, 694 (1st Cir. 1978); *IIT* v. *Cornfeld*, 619 F.2d 909, 928 (2d Cir. 1980); *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 452 (3d Cir. 1979); *O'Hara* v. *Kovens*, 625 F.2d 15, 18 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981); *Hudak* v. *Economic Research Analysts Inc.*, 499 F.2d 996, 999 (5th Cir.), cert. denied, 419 U.S. 1112 (1974); *Carothers* v. *Rice*, 633 F.2d 7, 12-15 (6th Cir. 1980), cert. denied, 49 U.S.L.W. 3710 (Mar. 23, 1981); *Cahill* v. *Ernst & Ernst*, 625 F.2d 151, 153 (7th Cir. 1980); *Vanderboom* v. *Sexton*, 422 F.2d 1233, 1237 (8th Cir.), cert. denied, 400 U.S. 852 (1970); *United California Bank* v. *Salik*, 481 F.2d 1012, 1014 (9th Cir.), cert. denied, 414 U.S. 1004 (1973);

Petitioners' reliance on *Occidental Life Ins. Co. of California* v. *EEOC*, 432 U.S. 355 (1977) for the proposition that state statutes of limitation should not be applied is wholly misplaced. *Occidental*, which is not a securities case, held that where the state statute of limitations was so short that it defeated the federal substantive policy, no statute of limitations would be applied at all. Hence, *Occidental* is not authority for borrowing federal statutes of limitations, but for rejecting all such statutes — a result that Petitioners hardly seek. Further, *Occidental* turned on the unique fact that the fundamental substantive federal policies of conciliation and voluntary settlement, on which Title VII of the Civil Rights Act was premised, would be defeated if a state one-year statute of limitations were imposed in Title VII cases. No remotely comparable situation is involved here.

3. Petitioners also urge that certiorari should be granted so that this Court can hold that only defrauded sellers but not defrauded purchasers, such as the plaintiffs, have a remedy under Section 10(b). In essence, they believe that the clock should be turned back 35 years and Section 10(b), the "judicial oak which has grown from little more than a legislative acorn" [*Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 737 (1975)], should be returned to its status as an acorn.

The arguments which Petitioners contrive, however, prove too much. There is no basis in the language of Section 10(b), its legislative history, or in the decisions interpreting it for distinguishing between defrauded purchasers and defrauded sellers. Either Petitioners must seek repeal of Section 10(b) altogether for victims of fraud, or they must urge that it be eviscerated without any regard to consistency or rational distinctions.

Mitchell v. *Texas Gulf Sulphur Co.*, 446 F.2d 90, 103 (10th Cir.), cert. denied, 404 U.S. 1004 (1971); *Forrestal Village, Inc.*, v. *Graham*, 551 F.2d 411, 413 (D.C. Cir. 1977).

Petitioners simply cannot escape the significance of this Court's repeated confirmation of a private claim for relief under Section 10(b).[9] The Court in these decisions was hardly unaware of the considerations on which Petitioners rely to deny a remedy here. The Court recognized a remedy under Section 10(b) because for 35 years, without the slightest hint of Congressional disapproval, lower court interpretations had made Section 10(b) the most important and widely utilized private remedy under the securities laws. This longstanding acceptance by the courts of the role of Section 10(b), coupled with Congress' failure to disturb these decisions, argued significantly in favor of continued recognition of a limited remedy under Section 10(b). It is this factor which distinguishes Section 10(b) from recent decisions in which this Court has declined to create *new* private rights of action under other sections of the federal securities laws.[10]

Indeed, only recently this Court recognized in connection with Section 10(b) that it "has frequently accepted a history of federal court recognition of a cause of action as indicative of the propriety of its implication." *Cannon* v. *University of*

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[9] See note 5, *supra*.

[10] Petitioners and the amicus mischaracterize this case as representative of an expansionist interpretation of the securities laws by the lower courts. The decision, however, is even more narrow than that of the Second Circuit in *Ross* v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980), in which this Court denied a petition for a writ of certiorari. In *Ross*, the Second Circuit recognized a claim for relief under Section 10(b) for misrepresentations in filed documents, the very documents which may give rise to Section 18(a) liability. Here, by contrast, the majority of the misrepresentations alleged were made in unfiled documents and orally, where Section 18(a) does not apply. The decision is also narrower than the Fifth Circuit's decision in *Huddleston* v. *Herman & MacLean*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 97,919 (1981). There, the court recognized a claim for relief under Section 10(b) for misrepresentations contained in a prospectus even though plaintiffs could have brought their claims under Section 11 of the Securities Act.

Chicago, 441 U.S. 677, 706 n.40 (1979). In *Touche Ross & Co.* v. *Redington, supra,* 442 U.S. at 577 n.19, the Court refused to accept the longstanding recognition of implied remedies under Section 10(b) as grounds for implying a similar remedy under Section 17(a) of the Securities Exchange Act because in the case of the latter, "There is no similar history of longstanding lower court interpretation in this case." The absence of such a longstanding history of lower court interpretation also provides a basis for distinguishing this Court's decision in *Transamerica Mortgage Advisors, Inc.* v. *Lewis, supra,* refusing to recognize an implied remedy for damages under Section 206 of the Investment Advisers Act of 1940.

The Court's treatment of Section 10(b) is consistent with its long-standing view that "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change." *Lorillard* v. *Pons,* 434 U.S. 575, 580 (1978). *See also, Andrus* v. *Allard,* 444 U.S. 51, 57 (1979); *Blue Chip Stamps* v. *Manor Drug Stores, supra,* 421 U.S. at 733-734; *Blau* v. *Lehman,* 368 U.S. 403, 413 (1962). Congress has revisited and amended the securities laws on countless occasions since it became evident that lower courts were implying private rights of action under Section 10(b). Not once did it suggest any disagreement with this approach of the courts.

Petitioners would like nothing more than for this Court to turn its back on four decades of judicial interpretation of Section 10(b) and to leave victims of one of the most massive stock frauds in the last decade without any remedy against persons who actively and knowingly participated in the fraud. There is no basis for such action in this Court's most recent decisions. In rejecting new private rights of action, the Court's decisions have nevertheless made clear that the Court has not abandoned the longstanding recognition of a private claim for relief for fraud under Section 10(b).

4. Petitioners and the amicus assert that this Court should grant certiorari to hold that claims may not be asserted under Section 10(b) against lawyers and accountants because such persons would be liable as "so-called aiders and abettors" and not as sellers of securities (Pet. 20). Such an assertion erroneously assumes that Petitioners are charged with liability under Section 10(b) as either sellers or aiders and abettors and in no other capacity. The attorneys and accountants in this case are charged in the complaint not only as aiders and abettors but also as principal violators who played a central role in the scheme to defraud and who themselves made material misrepresentations in connection with the sale of securities. Thus the issue raised by Petitioners — whether lawyers and accountants can be liable as aiders and abettors under Section 10(b) — is prematurely raised. When Respondents have their day in court, it may well be that aiding and abetting plays no role at all in this case.

Petitioners claim that there is no statutory basis in Section 10(b) for prohibiting fraud by accountants and attorneys who are not sellers. They ignore the very obvious statutory basis: Section 10(b) is not limited to sellers; it proscribes conduct by "any person" who "directly or indirectly" engages in the prohibited conduct. There is no special exemption for lawyers and accountants from the definition of "person."[11]

Petitioners would have this Court ignore the literal language of the statute because of purported concern about the danger of vexatious litigation against attorneys and accountants. Such a concern is especially ironic in this case. This is a case in which the two individual accountants were criminally prosecuted, in which all of the Petitioners were

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[11] Section 3(a)(9) of the Act defines person to include "a natural person." Further, Section 18(a) of the Act, which also relies on "any person" language, was originally drafted to cover "any person (including any director or officer, or any accountant or other expert.)" The parenthetical clause was deleted in conference because "[t]he words in parentheses are . . . superfluous." H.R. Conf. Rep. 1838, 73rd Cong., 2d Sess. 36 (1934).

subject to SEC enforcement proceedings, and in which all consented to judgments against them. Further, a district court opinion and an appellate opinion in related cases strongly suggest egregious fraud by these same Petitioners. Nevertheless, these Petitioners criticize the Plaintiffs — all institutional investors which for the most part are acting in a representative capacity — for bringing a vexatious action and in the same breath attempt to bar this action as untimely because Petitioners investigated and deliberated too long before filing suit.

Finally, there is no circuit court conflict on the issues that Petitioners seek to raise. Petitioners are unable to point to a single decision supporting their contention that Section 10(b) affords a special dispensation to professionals who engage in fraudulent conduct or even that aiding and abetting liability does not lie under Section 10(b).

5. In the court of appeals, the accounting Petitioners argued that "If the 1934 Act Applies, an Implied Right of Action under §10(b) Does Not Lie Since the Conduct in Issue Is Subject to §18 [of the Securities Exchange Act]" (PMM Br. 68). Now, both the accounting Petitioners and the amicus AICPA argue that because Section 18(a) does not provide a remedy to Respondents, no claim can be stated under Section 10(b). That is why the court of appeals characterized Petitioners' arguments as a "Catch 22." Petitioners believe that if the express provisions provide a remedy for the fraud, then the victims of the fraud should not be permitted to proceed under Section 10(b), but if the express provisions do not provide a remedy for the fraud, that is even more reason to deprive them of a remedy under Section 10(b).

Petitioners' argument rests on a misunderstanding of the different purposes served by Section 18(a) and Section 10(b). Section 18(a) provides a remedy for deception resulting from eyeball reliance on documents filed with the SEC. See, e.g., *Ross* v. *A.H. Robins Co.*, 607 F.2d 545, 552 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980). It is designed to insure the integrity of corporate reports filed with the SEC and relied

upon by purchasers of securities. In contrast, Section 10(b) is not designed to protect the integrity of filed documents; it is designed to protect against frauds perpetrated on purchasers and sellers of securities through false representations, which are often made in unfiled documents and in oral statements. Thus, Section 18(a) does not, as Petitioners argue, serve to insulate from Section 10(b) liability persons who choose to defraud the public through, for example, press releases, public announcements and reports disseminated to investors that are not required to be filed with the SEC.

Further, Petitioners' argument that Section 10(b) cannot be used where a Section 18(a) claim does not lie is refuted by the decisions of this Court recognizing Section 10(b) claims where filed documents were not even at issue. See *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972); *Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6 (1971). The reliance of the complaint principally on false representations disseminated in unfiled documents removes any doubt that a claim for relief is stated under Section 10(b).

Nor is it significant that some of the misrepresentations made in unfiled documents were also made in filed documents. Section 18(a) requires eyeball reliance on the filed documents. *Ross* v. *A.H. Robins Co., supra,* 607 F.2d at 552; *Heit* v. *Weitzen,* 402 F.2d 909, 916 (2d Cir. 1968), cert. denied, 395 U.S. 903 (1969). Persons who are defrauded through widely disseminated fraudulent unfiled documents are not deprived of a Section 10(b) remedy simply because they did not read the filed documents containing the same misrepresentations. And, even if there were some overlap in remedies afforded by Section 10(b) and Section 18(a) — a factor which is not present in this case to the extent no reliance is claimed on the filed misrepresentations — the Section 10(b) claim would not be defeated. As this Court repeatedly has recognized, the fact that there may be some overlap between the various provisions of the securities laws is neither unusual nor unfortunate. *United States* v. *Naftalin,* 441 U.S. 768,778

(1979); *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 390-391 (1970): *SEC* v. *National Securities Co.*, 393 U.S. 453, 468 (1969).

6. Petitioners in No. 80-1802 urge that even if small unsophisticated investors would have a remedy under Section 10(b), in the circumstances of this case Respondents should not because they are "sophisticated institutional investors" (Pet. 4). Petitioners ignore, however, that the protections and remedies of the securities laws "are not accorded only to those who fail a battery of information and intelligence tests, but are simply conditioned upon the misrepresentation of material facts." *Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville,* 409 F.2d 989, 992 (5th Cir. 1969). There is no statutory or decisional support for Petitioners' wholly impractical interpretation of Section 10(b). To the contrary, this Court's decisions make abundantly clear that the antifraud proscriptions of the securities laws are as much for the protection of the sophisticated as for the unsophisticated. See, e.g., *Rubin* v. *United States,* 101 S.Ct. 698 (1981); *United States* v. *Naftalin,* 441 U.S. 768 (1979).

In *Naftalin,* this Court recognized that "the welfare of investors and financial intermediaries are inextricably linked — frauds perpetrated upon either business or investors can redound to the detriment of the other and to the economy as a whole." 441 U.S. at 776. Here, Respondents purchased for the most part as trustees for numerous small unsophisticated investors. Whatever restrictions are placed on Section 10(b) ultimately will redound to the detriment of such investors.[12]

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[12] Petitioners in No. 80-1684 seek to raise the question whether a private claim for relief may be stated under Section 17(a) of the Securities Act. The court of appeals, however, did not decide that question, and it is therefore inappropriate for consideration on a writ of certiorari. *NLRB* v. *Sears, Roebuck & Co,* 421 U.S. 132, 163-164 (1975); *Ramsey* v. *United Mine Workers,* 401 U.S. 302, 312 (1971).

7. Petitioners urge that certiorari should be granted to determine whether the court of appeals erred in refusing to apply its decision in *Forrestal Village Inc.* v. *Graham,* 551 F.2d 411 (D.C. Cir. 1977) retroactively. That decision held that the D.C. two-year blue sky statute of limitations, rather than the three year general fraud limitation, applies to Section 10(b) cases.

The issue raised by Petitioners is not worthy of certiorari. Supreme Court resolution of this issue would have no effect on future cases because the law on the statute of limitations question has changed drastically in the last decade. The court of appeals decision was premised on the fact that as of December 1971 — the time the district court found the two year blue sky limitation period expired for Plaintiffs in this action — forty-six of forty-eight federal court decisions had applied the forum state's general fraud statute to Section 10(b) actions[13], and this was the law in the District of Colum-

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[13] The court of appeals relied upon the following pre-1972 decisions: *First Circuit: Janigan* v. *Taylor,* 344 F.2d 781, cert. denied, 382 U.S. 879 (1965); *Second Circuit: Klein* v. *Auchincloss, Parker & Redpath* 436 F.2d 339 (1971); *Klein* v. *Bower,* 421 F.2d 338 (1970); *Moerman* v. *Zipco, Inc.,* 302 F. Supp. 439 (E.D.N.Y. 1970), *aff'd per curiam,* 422 F.2d 871 (1970); *Fischman* v. *Raytheon Manufacturing Co.,* 188 F.2d 783 (1951); *Weinberger* v. *New York Stock Exchange,* 335 F.Supp. 139 (S.D.N.Y. 1971); *Klein* v. *Spear, Leeds & Kellogg,* 306 F.Supp. 743 (S.D.N.Y. 1969); *Saylor* v. *Lindsley,* 302 F.Supp. 1174 (S.D.N.Y. 1969); *Marth* v. *Industrial Incomes Incorporated of North America,* 290 F.Supp. 755 (S.D.N.Y. 1968); *Shapiro* v. *Schwamm,* 279 F.Supp. 798 (S.D.N.Y. 1968); *Maher* v. *J.R. Williston & Beane, Inc.,* 280 F.Supp. 133 (S.D.N.Y. 1967); *Glickman* v. *Schweickart & Co.,* 242 F.Supp. 670 (S.D.N.Y. 1965); *Dack* v. *Shanman,* 227 F.Supp. 26 (S.D.N.Y. 1964); *Osborne* v. *Mallory,* 86 F.Supp. 869 (S.D.N.Y. 1949); *Third Circuit: Tobacco & Allied Stocks, Inc.* v. *Transamerica Corp.,* 143 F.Supp. 323 (D. Del. 1956), aff'd without consideration of the point, 244 F.2d 902 (1957); *Fourth Circuit: Stevens* v. *Abbott, Proctor & Paine,* 288 F.Supp. 836 (E.D.Va. 1968); *Baumel* v.

bia (ibid). Thus, the court noted that "prior to, and during, the running of the limitations period, federal courts, including this circuit, overwhelmingly adopted the general fraud limita-

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Rosen, 283 F.Supp. 128 (D. Md. 1968); *Fifth Circuit: Bailes* v. *Colonial Press, Inc.,* 444 F.2d 1241 (1971); *Aboussie* v. *Aboussie,* 441 F.2d 150 (1971); *Weiser* v. *Shwartz,* 286 F.Supp. 389 (E.D.La. 1968); *Azalea Meats, Inc.,* v. *Muscat,* 246 F.Supp. 780 (S.D.Fla. 1965), rev'd on other grounds, 386 F.2d 5 (1967); *Hooper* v. *Mountain States Securities Corp.,* 282 F.2d 195 (1960), cert. denied, 365 U.S. 814 (1961); *Carpenter* v. *Hall,* 311 F.Supp. 1099 (S.D.Tex. 1970); *Hendricks* v. *Flato Realty Investments,* [1967-1969 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 92,290 (S.D.Tex. 1968); *Sixth Circuit: Charney* v. *Thomas,* 372 F.2d 97 (1967); *Connelly* v. *Balkwill,* 174 F.Supp. 49 (N.D. Ohio, 1959), aff'd per curiam, 279 F.2d 685 (1960); *Denny* v. *Performance Systems, Inc.,* [1971-1972] Fed.Sec.L.Rep. (CCH) ¶ 93,387 (M.D. Tenn. 1971); *Dudley* v. *Allen* [1971-1972] Fed.Sec.L.Rep. (CCH) ¶ 93,273 (W.D. Ky. 1971); *Seventh Circuit: Morgan* v. *Koch,* 419 F.2d 993 (1969); *Butterman* v. *Steiner,* 343 F.2d 519 (1965); *Schaefer* v. *First National Bank of Lincolnwood,* 326 F.Supp. 1186 (N.D. Ill. 1971); *Northern Trust Co.* v. *Essaness Theatres Corp.,* 103 F.Supp. 954 (N.D. Ill. 1952); *Ninth Circuit: Douglass* v. *Glenn E. Hinton Investments, Inc.,* 440 F.2d 912 (1971); *Sackett* v. *Beaman,* 399 F.2d 884 (1968); *Hecht* v. *Harris, Upham & Co.,* 283 F.Supp. 417 (N.D.Cal. 1968), modified on other grounds, 430 F.2d 1202 (1970); *Turner* v. *Lundquist,* 377 F.2d 44 (1967); *Royal Air Properties, Inc.,* v. *Smith,* 312 F.2d 210 (1962); *Errion* v. *Connell,* 236 F.2d 35 (1971); *Fratt* v. *Robinson,* 203 F.2d 627 (1953); *Smith* v. *Guaranty Service Corp.,* 51 F.R.D. 289 (N.D. Cal. 1970); *Tenth Circuit: Richardson* v. *MacArthur,* 451 F.2d 35 (1971); *Mitchell* v. *Texas Gulf Sulphur Company,* 446 F.2d 90, cert. denied, 404 U.S. 1004 (1971); *deHaas* v. *Empire Petroleum Co.,* 435 F.2d 1223 (1970); *Chiodo* v. *General Waterworks Corp.,* 380 F.2d 860, cert. denied, 389 U.S. 1004 (1967); *Geo. H. McFadden & Brothers* v. *Home-Stake Production Co.,* 295 F.Supp. 587 (N.D. Okla. 1968); *Trussell* v. *United Underwriters, Ltd.,* 228 F.Supp. 757 (D. Colo. 1964). As late as 1975, courts in the D.C. Circuit reaffirmed that the three-year general fraud limitation applies to Section 10(b) action. See, e.g., *Vance* v. *National Realty Trust,* [1974-1975] Fed.Sec.L.Rep. (CCH) ¶ 95,004 (D.C. Cir. 1975); *National Realty Trust* v. *Neelon Management*

tion period" (Pet. App. A-13). This was the basis for its determination that, as to the Plaintiffs in this action, *Forrestal Village* established a new principle of law. It was also the basis for its conclusion that it would be inequitable to hold that Respondents slept on their rights since at the time they filed their complaint the three-year statute of limitations clearly applied.

Since 1971 the lower courts have reconsidered the question, and the certainty that existed a decade ago has disappeared. In the last decade the lower courts have divided sharply on whether state blue sky or fraud limitations apply to Section 10(b) actions.[14] As a result, no plaintiff filing a complaint today or even in the last five years could claim, as was the case here, that a decision applying a blue sky limitation period was wholly unforeshadowed or marked a sharp departure from earlier decisions. Thus, this Court's resolution of the issue posed by Petitioners would be limited to the facts and the parties in this particular case.

Further, the court of appeals decision is correct on the merits. This case is at least as compelling for nonretroactivity as *Chevron Oil Co.* v. *Huson* 404 U.S. 97 (1971). *Chevron*, like the instant case, involved the question whether retroactive application should be given to a decision that effectively applied a state one-year limitation period to actions for injuries sustained on the Outer Continental Shelf. The Court found

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Co., [1973] Fed.Sec.L.Rep. ¶ 94,049 (D.D.C. 1973); *Conlow* v. *University Computing Co.*, [1972-1973] Fed.Sec.L.Rep. (CCH) ¶ 93,796 (D.D.C. 1973).

[14] Compare, e.g., *O'Hara* v. *Kovens*, 625 F.2d 15 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981); *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977); *Berry Petroleum Co.* v. *Adams & Peck*, 518 F.2d 402 (2d Cir. 1975); *Parrent* v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972) (applying blue sky limitation periods) with, e.g., *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450 (3rd Cir. 1979) and *Cook* v. *Avien, Inc.*, 573 F.2d 685 (1st Cir. 1978) (applying general fraud limitation periods).

that the decision should be applied prospectively because (1) it overruled prior law on which plaintiff had relied in determining when to bring the action; (2) it would undermine the protective purposes of the statute in issue to deprive an injured person of a remedy on the basis of superseding legal doctrine that was not foreseeable; and (3) it would be substantially inequitable to hold that the plaintiff had slept on his rights since at the time he filed his action the existing law was that his action was timely. Quoting from an earlier decision, this Court emphasized that "[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity." *Id.* at 107.

In the decision below, the court of appeals found, as in *Chevron,* that its *Forrestal Village* decision changed the law in the D.C. Circuit as it existed at the time Respondents filed their complaint. It also found that it would be substantially inequitable to hold that Respondents slept on their rights on the basis of a decision rendered four years after they filed their complaint. Petitioners complain that the court below did not also find that the second factor mentioned in *Chevron* had been met. The second factor was in fact met: the purposes of the securities laws are indeed undermined when victims of fraud are deprived of a remedy on the basis of unforeseen changes in the law. In any event, *Chevron* only requires that the three factors be "considered," not that each be met. 404 U.S. at 106.

Finally, the decision of the court of appeals does not create any conflict with the decisions of any other court of appeals. The attorney Petitioners rely on *Schaefer* v. *First National Bank of Lincolnwood,* 509 F.2d 1287 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976). That case, however, was brought in the Seventh Circuit and the Seventh Circuit held that the decision in question did not overturn prior law in the Seventh Circuit. 509 F.2d at 1294-1295. Here the action was brought in the District of Columbia and the D.C. Circuit

specifically found that its *Forrestal Village* decision did overturn prior D.C. Circuit law. Further, in *Schaefer* retroactive application of the statute of limitations had little effect on plaintiffs' claims; more than two dozen defendants remained in the case even under the shorter statute of limitations. Here, application of the shorter statute of limitations would defeat Respondents' claims in their entirety.

The accounting Petitioners attempt to create a conflict in the circuits by relying upon *Valencia* v. *Anderson Brothers Ford,* 617 F.2d 1278 (7th Cir.), cert. granted, 101 S.Ct. 395 (1980) and *Holzsager* v. *The Valley Hospital,* No. 80-7839 (2d Cir. Apr., 1981). They ignore, however, that a conflict can justify review only if there is "a real conflict on the same matter of law or fact, not merely an inconsistency in *dicta* or in the general principles utilized." R. Stern & E. Gressman, Supreme Court Practice 264 (5th ed. 1978).

The decisions on which the accounting Petitioners rely are not even securities decisions, much less Section 10(b) decisions, and they raise no issues regarding retroactive application of statutes of limitations decisions. *Valencia* held only that a particular interpretation of the Truth in Lending Act would be applied retroactively because, unlike this case, the court concluded that the interpretation was supported by the weight of prior authority. The suggestion that all three *Chevron* factors must be met was only in *dicta,* and unlike in *Valencia,* where the court did not find that any of the *Chevron* factors had been met, all three factors were in fact met here. *Holzsager* applied a jurisdictional decision retroactively even though that decision changed existing law, but as the concurring judge noted in that case, jurisdictional decisions have always been applied retroactively [citing this Court's decision in *Firestone Tire & Rubber Co.* v. *Risjord,* 49 U.S.L.W. 4089, 4092 (Jan. 13, 1981)].

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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